

Office of Chief Counsel  
Internal Revenue Service

**memorandum**

CC:LM:MCT:DET:POSTF-149633-01

RLCarroll

date: OCT 26 2001

to: Teresa L. Beumel, Team Manager, 1556  
Livonia, MI

from: Phoebe L. Nearing  
Associate Area Counsel, Large and Mid-Size Business - Michigan

---

subject: [REDACTED] - [REDACTED] Refund Decrease and [REDACTED] Deficiency from [REDACTED] NOL  
carryback to [REDACTED]

This memorandum responds to your request for assistance dated August 29, 2001 and should not be cited as precedent. This memorandum modifies and supplements the draft memorandum we provided to you on October 15, 2001.

**ISSUES**

1. In determining the income tax overpayment attributable to a net operating loss carryback that may be refunded or credited, should the taxable income of the carryback year be increased by the amount of an adjustment upon which the taxpayer previously paid unassessed tax when the assessment is now barred by the period of limitations.
2. May a deficiency be assessed on an otherwise time-barred tax year when the deficiency was generated by a decrease in a minimum tax credit carryover created by an alternative minimum tax net operating loss carryback to a previous tax year.

**CONCLUSIONS**

1. Yes. In determining the amount of an overpayment that may be refunded or credited, the taxable income of the carryback year should be increased by the amount of an adjustment upon which the taxpayer previously paid tax that was never assessed but is now barred by the period of limitations.
2. Yes. A deficiency may be assessed on an otherwise time-barred tax year when the deficiency was generated by a decrease in a minimum tax credit carryover created by an alternative minimum tax net operating loss carryback to a previous tax year.

## FACTS

On [REDACTED], [REDACTED] and its subsidiaries ("[REDACTED]") filed Form 1120X, Amended U.S. Corporation Income Tax Return, for its tax year ended March 31, [REDACTED] ("original [REDACTED] 1120X"). The original [REDACTED] 1120X was filed to carryback a net operating ("NOL") loss from its tax year ended March 31, [REDACTED] and to show an increase in income and a decrease in deductions from [REDACTED]. These changes created an increase in alternative minimum tax ("AMT") for tax year ended March 31, [REDACTED] ("tax year [REDACTED]"), resulting in a tax deficiency of \$[REDACTED]. [REDACTED] paid this amount when it filed its original [REDACTED] 1120X. The Cincinnati Service Center filed [REDACTED]'s original [REDACTED] 1120X but did not assess the tax. The statute of limitations for assessing the tax related to the original [REDACTED] 1120X expired on December 15, [REDACTED].

[REDACTED] reflected a \$[REDACTED] NOL on its Form 1120 filed for its tax year ended March 31, [REDACTED] ("tax year [REDACTED]"). Consequently, on [REDACTED], [REDACTED] filed another Form 1120X for tax year [REDACTED] ("second [REDACTED] 1120X") to carryback that \$[REDACTED] NOL. This resulted in a \$[REDACTED] decrease in tax for tax year [REDACTED]. This also resulted in a decrease of \$[REDACTED] in the amount of the AMT credit ("MTC") available for carryover to tax year ended March 31, [REDACTED] ("tax year [REDACTED]").

Due to the decrease in MTC available for carryover, [REDACTED] was required to file a second Form 1120X for tax year [REDACTED] ("second [REDACTED] 1120X"). Note: An earlier Form 1120X was filed for tax year [REDACTED] to reflect the tax consequences resulting from the carryback of the [REDACTED] NOL to tax year [REDACTED]. On its second [REDACTED] 1120X, [REDACTED] reflected a \$[REDACTED] increase in tax, thus creating a deficiency. However, the statute of limitations for assessing the tax related to taxable year [REDACTED] expired prior to the filing of the [REDACTED] 1120X.

Previous advice by our office indicated that neither a closing agreement pursuant to I.R.C. § 7121, nor mitigation pursuant to I.R.C. §§ 1311 through 1314, would be appropriate to effect an assessment of the tax reported on the original [REDACTED] 1120X.

The Examination Division now wants to use the deficiency from the original [REDACTED] 1120X to offset the refund claimed on the second [REDACTED] 1120X. Furthermore, the Examination Division wants to assess the tax owed by [REDACTED] pursuant to the [REDACTED] 1120X.

## DISCUSSION AND ANALYSIS

### ISSUE 1:

Previous advice provided by this office indicated that the inability to make a deficiency assessment in a prior year (from which MTC carryforwards originate) does not prevent taking into account the deficiency in determining an overassessment in a subsequent year. Likewise, the inability to make a deficiency assessment in a prior year does not prevent taking into account the deficiency in determining an overassessment for that year.

In Rev. Rul. 81-88, the Service stated that in accordance with Treas. Reg. § 301.6511(d)-2(a)(3), if an NOL is carried back to a year in which there is a barred adjustment that would increase taxable income, that adjustment will be made as a set-off against the NOL. See also Commissioner v. Van Bergh, 209 F.2d 23 (2d Cir. 1954); Phoenix Coal Co. v. Commissioner, 231 F.2d 420 (2d Cir. 1956).

In Lewis v. Reynolds, 284 U.S. 281 (1932), the Commissioner audited petitioner's return and assessed a deficiency. Petitioner paid the deficiency and asked for a refund. The Commissioner denied this request and issued a revised computation that allowed some previously denied deductions, but showed a greater tax liability than before. The Supreme Court held that the Commissioner had the authority in acting upon a claim for refund to redetermine and reassess the tax after the statute of limitations ran. The Court stated that a claim for refund involves a redetermination of the entire tax liability, and that while no new assessment can be made after the statute of limitations had expired, the taxpayer is not entitled to a refund unless there has been an overpayment of tax.

Section 6401 of the Internal Revenue Code defines an "overpayment" as a payment assessed or collected after the expiration of the period of limitations. The Service has taken the position that an amount paid before the expiration of the period of limitations on assessment but assessed after the expiration of the period of limitations on assessment is not an overpayment within the meaning of §6401. Rev. Rul. 85-67, 1985-1 C.B. 364. Moreover, the assessment does not create the liability; a taxpayer can be liable for a tax and make a payment for that tax even though the tax is not assessed. Id.; see also Ewing v. United States, 914 F.2d 499 (4th Cir. 1990).

In the situation presented, the taxpayer owed \$ [REDACTED] in tax for tax year [REDACTED] and paid that amount prior to the expiration of the period of limitations on assessment. Thus, although the Service cannot now assess the \$ [REDACTED] because the period of limitations on assessment has expired, the taxpayer is not entitled to recover that amount; the taxpayer is only entitled to a refund of money that properly belongs to it. The second [REDACTED] 1120X filed by the taxpayer claimed a refund of \$ [REDACTED], an amount

that had already taken into account the \$ [REDACTED] liability properly owed to the government. If the taxpayer had not taken that liability into account when it filed the second [REDACTED] 1120X, but instead had claimed a refund of \$ [REDACTED], the taxpayer would still only be entitled to a refund of \$ [REDACTED] because that was all that had been overpaid.

In this case, the taxpayer filed a claim for refund on its second [REDACTED] 1120X. In a claim for refund, the Commissioner has the authority to redetermine the entire tax liability. See Lewis, above. Because the NOL carryback from tax year [REDACTED] created a refund or credit, the time-barred adjustment for the unassessed tax for taxable year [REDACTED] can be made as a setoff against the NOL in determining the amount of the refund or credit for tax year [REDACTED].

## ISSUE 2:

Internal Revenue Code § 6501(a) provides that the amount of any tax imposed by this title shall be assessed within three years after the return is filed. I.R.C. § 6501(h) provides that in the case of a deficiency attributable to the application to the taxpayer of an NOL carryback, such deficiency may be assessed at any time before the expiration of the period within which a deficiency for the tax year of the NOL which results in such carryback may be assessed.

Internal Revenue Code § 55 provides for an alternative minimum tax that is imposed on a taxpayer's taxable income as recomputed to adjust for certain tax preference items. AMT paid in excess of the AMT due may be carried over as a credit (alternative minimum tax credit or "MTC") against AMT imposed in subsequent years.

The deficiency for tax year [REDACTED] resulted from the reduction in the MTC carryover from tax year [REDACTED] that was applied in tax year ended March 31, [REDACTED]. The MTC carryover is attributable to the NOL from tax year [REDACTED] because the NOL from tax year [REDACTED] was carried back to decrease the taxable income for tax year [REDACTED] and correspondingly decreased the MTC carryover from tax year [REDACTED].

An NOL generally generates a credit or a refund, but in this case an NOL carryback resulted in a deficiency because the NOL carryback reduced the amount of the MTC that could be carried over and applied to a subsequent tax year.

Because the deficiency sought to be assessed is attributable to the carryback of an NOL (which resulted in a decrease in an MTC carryover), the statute of limitations for assessing the tax due to the MTC carryover decrease would be three years from the date of filing the return for tax year [REDACTED].

Assuming the three-year assessment period for the return filed for tax year [REDACTED]

has not expired, the deficiency resulting from the adjustment in tax for tax year [REDACTED] (from the decrease in MTC carryover resulting from the NOL carryback from tax year [REDACTED] to tax year [REDACTED]) may still be assessed.

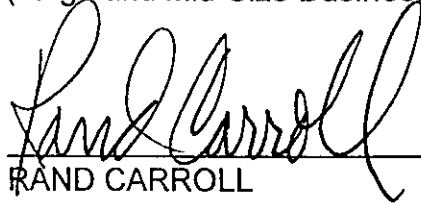
Should you have any questions or concerns regarding this matter, please contact the undersigned attorney at 313/237-6436.

**DISCLOSURE STATEMENT**

**This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.**

PHOEBE L. NEARING  
Associate Area Counsel  
(Large and Mid-Size Business)

By:

  
RAND CARROLL  
Attorney (LMSB)